Hydro Québec

Quarterly Report

Second Quarter 2007

Message from the Chairman of the Board and the President and Chief Executive Officer

Summary of results

For the six months ended June 30, 2007, income from continuing operations totaled $2,045 million, or $330 million more than for the first six months of last year. This increase is mainly due to growth in net electricity exports by Hydro-Québec Production, which accounted for $362 million, colder temperatures in 2007 than in 2006, which accounted for $164 million, and a positive variance of $142 million in net revenue from special contracts with large-power industrial customers. These factors were mitigated by the introduction, in January 2007, of water-power royalties payable by Hydro-Québec Production to the Québec government, for $143 million. It should also be noted that a $234-million non-recurring foreign exchange gain was recognized in second quarter 2006 on debts and swaps denominated in U.S. dollars.

Income from discontinued operations was $21 million, compared to $856 million in 2006. The 2007 income resulted primarily from an $18-million gain on the sale of our interest in DirectLink (Australia) in the first quarter. In the second quarter of 2006, the sale of our interest in Transelec (Chile) had generated a gain of $806 million, revalued at $813 million in third quarter 2006 after the release of Transelec's final financial statements as at June 30, 2006.

For the six months ended June 30, 2007, net income totaled $2,066 million, as against $2,571 million in 2006.

Income from continuing operations for second quarter 2007 reached $635 million, up $25 million from 2006. This result is mainly attributable to a $228-million increase in Hydro-Québec Production's net electricity exports in 2007, offset by the $234-million non-recurring exchange gain recognized in 2006 on debts and swaps denominated in U.S. dollars.

Consolidated results

Revenue for the first six months of 2007 amounted to $6,560 million, a year-over-year increase of $766 million. Revenue from electricity sales rose by $1,009 million to $6,379 million. For the Québec market, the total was $5,412 million, up $602 million over 2006. Sales on markets outside Québec generated $967 million, an increase of $407 million. Other revenue was down, primarily because of the recognition on June 30, 2006, of the $234-million non-recurring foreign exchange gain on debts and swaps denominated in U.S. dollars.

In Québec, the $602-million increase in revenue from electricity sales was chiefly due to colder temperatures in 2007, growth in revenue from special contracts with large-power industrial customers, and rate adjustments effective April 1, 2006 and 2007.

On markets outside Québec, the $407-million increase was primarily attributable to a higher volume of exports by Hydro-Québec Production and, to a lesser extent, the resale of excess supply by Hydro-Québec Distribution.

Total expenditure was $3,308 million, or $311 million more than in 2006. The difference stems mainly from a $169-million increase in electricity purchases in excess of the heritage pool and the introduction, in January 2007, of water-power royalties payable by Hydro-Québec Production to the Québec government, for $143 million.

Financial expenses were $1,207 million, up $125 million over 2006. The difference is in part attributable to higher interest rates on capital markets. In addition, the application of new accounting standards for financial instruments, which abolish the transitional rules granted in 2004, gave rise to an upward adjustment of retained earnings as at January 1, 2007, and consequently terminated the amortization of a deferred gain.

Segmented results

Generation

For the first six months of 2007, Hydro-Québec Production posted net income of $1,410 million, up $68 million from the same period last year. The difference is mainly owing to the growth in net electricity exports and the increase in net revenue from special contracts with large-power industrial customers. These factors were largely offset by the introduction of water-power royalties in January 2007 and by the recognition, during second quarter 2006, of the $234-million non-recurring foreign exchange gain on debts and swaps denominated in U.S. dollars.

Transmission

Hydro-Québec TransÉnergie's net income amounted to $277 million for the first half of the year, a decrease of $150 million from last year.

Revenue was $1,409 million, down $94 million from $1,503 million in 2006. Following a decision handed down by the Régie de l'énergie in April 2006, non-recurring native load transmission revenue of $170 million for 2005 had been recognized in revenue for second quarter 2006. This has resulted in a year-over-year reduction of $170 million in 2007, which was partially offset by additional income of $28 million approved by the Régie in a 2007 decision and by a $46-million increase in revenue generated by point-to-point transmission services, essentially attributable to the increase in Hydro-Québec Production's exports.

Distribution

Hydro-Québec Distribution posted net income of $372 million, versus a $48-million loss in the first six months of 2006, a $420-million improvement. This increase is mainly due to higher revenue from electricity sales and a reduction in the cost of native load transmission service stemming from the fact that $170 million in non-recurring transmission costs for 2005 had been recorded in second quarter 2006. These factors were partially offset by a higher volume of electricity purchases in excess of the heritage pool.

Revenue from electricity sales totaled $5,403 million, up $593 million over last year, basically because of colder temperatures in the first six months of 2007, the increase in revenue from special contracts with large-power industrial customers, and the April 2006 and 2007 rate adjustments. It should be noted that all risks related to special contracts are assumed by Hydro-Québec Production. Sales volume was 90.1 TWh, an increase of 3.1 TWh attributable mainly to colder temperatures.

Construction

The Construction segment comprises the operations of Hydro-Québec Équipement and Société d'énergie de la Baie James.

For the first six months, the volume of activity totaled $823 million, compared to $838 million in 2006. As in 2006, several major projects are being carried out for Hydro-Québec Production and Hydro-Québec TransÉnergie. Noteworthy among them is the Eastmain-1-A/Sarcelle/Rupert project, which got under way in the first quarter of 2007.

Investment

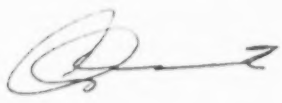
As at June 30, 2007, investments in fixed and intangible assets and in the implementation of the Energy Efficiency Plan totaled $1,495 million, compared to $1,468 million in 2006. As anticipated, a large portion of this amount was devoted to the development projects of Hydro-Québec Production, such as the Eastmain-1-A/Sarcelle/Rupert project and the Péribonka, Chute-Allard and Rapides-des-Cœurs hydroelectric developments.

Hydro-Québec TransÉnergie continued expanding its transmission system to accommodate new generating capacity. Hydro-Québec Distribution continued to invest in order to meet growth in demand and improve service quality, notably through the Customer Information System project, while pursuing deployment of the Energy Efficiency Plan.

Financing

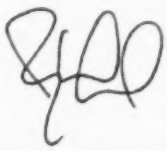
The 2007 borrowing program amounts to $1.1 billion, a relatively modest amount compared to previous years, mainly because of funds available from the disposal of our foreign holdings, which was completed at the end of February 2007. The proceeds from our borrowings will be used to refinance debt maturing this year and to finance the investment program.

No borrowings were made during the second quarter. A single, $526-million borrowing has been made since the beginning of the year. It was contracted on the Canadian market at a cost of 4.73%.



Michael L. Turcotte

Chairman of the Board



Thierry Vandal

President and Chief Executive Officer

August 17, 2007

CONSOLIDATED STATEMENTS OF OPERATIONS

In millions of Canadian dollars
(unaudited)

	Notes	Three months ended June 30		Six months ended June 30	
		2007	2006	**2007**	2006
Revenue		**2,828**	2,595	**6,560**	5,794
Expenditure					
Operations		**617**	564	**1,223**	1,123
Electricity and fuel purchases		**337**	284	**759**	647
Depreciation and amortization	4	**477**	496	**959**	985
Taxes		**187**	89	**395**	242
Regulatory deferrals	3	**(14)**	-	**(28)**	-
		1,604	1,433	**3,308**	2,997
Operating income		**1,224**	1,162	**3,252**	2,797
Financial expenses	5	**589**	552	**1,207**	1,082
Income from continuing operations		**635**	610	**2,045**	1,715
Income from discontinued operations	6	**-**	832	**21**	856
Net income		**635**	1,442	**2,066**	2,571

CONSOLIDATED STATEMENTS OF RETAINED EARNINGS

In millions of Canadian dollars
(unaudited)

	Note	Three months ended June 30		Six months ended June 30	
		2007	2006	**2007**	2006
Balance at beginning of period		**16,203**	14,204	**14,474**	13,075
Adjustments related to the adoption of new accounting policies	2	**-**	-	**298**	-
Net income		**635**	1,442	**2,066**	2,571
Balance at end of period		**16,838**	15,646	**16,838**	15,646

The accompanying notes are an integral part of the consolidated financial statements.

CONSOLIDATED BALANCE SHEETS

In millions of Canadian dollars

	Notes	As at June 30, 2007 (unaudited)	As at December 31, 2006 (audited)
ASSETS			
Current assets			
Cash and cash equivalents		**1,142**	52
Short-term investments		**149**	3,178
Accounts receivable		**1,819**	1,597
Derivative instruments		**1,089**	1,491
Materials, fuel and supplies		**383**	365
Assets held for sale	6	**-**	11
		4,582	6,694
Property, plant and equipment		**52,226**	51,813
Investments		**221**	232
Derivative instruments		**1,660**	1,093
Intangible assets		**923**	923
Other assets		**2,300**	2,462
Assets held for sale	6	**-**	31
		61,912	63,248
LIABILITIES			
Current liabilities			
Borrowings		**65**	25
Accounts payable and accrued liabilities		**1,469**	1,818
Dividends payable		**-**	2,342
Accrued interest		**837**	936
Regulatory liability		**143**	251
Current portion of long-term debt		**1,009**	1,063
Derivative instruments		**475**	340
Liabilities related to assets held for sale	6	**-**	1
		3,998	6,776
Long-term debt		**32,193**	33,027
Derivative instruments		**2,419**	1,111
Asset retirement obligations		**450**	431
Other long-term liabilities		**681**	2,719
Long-term liabilities related to assets held for sale	6	**-**	7
Perpetual debt		**309**	337
		40,050	44,408
SHAREHOLDER'S EQUITY			
Share capital		**4,374**	4,374
Retained earnings		**16,838**	14,474
Accumulated other comprehensive income	8	**650**	(8)
		17,488	14,466
		21,862	18,840
		61,912	63,248
Commitments and contingencies	11		

The accompanying notes are an integral part of the consolidated financial statements.

CONSOLIDATED STATEMENTS OF CASH FLOWS

In millions of Canadian dollars
(unaudited)

	Notes	Three months ended June 30		Six months ended June 30	
		2007	2006	**2007**	2006
Operating activities					
Net income		**635**	1,442	**2,066**	2,571
Income from discontinued operations	6	**-**	(832)	**(21)**	(856)
Income from continuing operations		**635**	610	**2,045**	1,715
Adjustments					
Depreciation and amortization	4	**477**	496	**959**	985
Amortization of debt premiums, discounts and issue expenses	5	**34**	25	**61**	51
Exchange gain		**(73)**	(387)	**(89)**	(397)
Difference between contributions paid and pension cost		**75**	(41)	**147**	(48)
Regulatory deferrals		**(14)**	-	**(28)**	-
Other		**37**	(13)	**80**	(42)
Change in non-cash working capital items	9	**719**	625	**(708)**	(620)
		1,890	1,315	**2,467**	1,644
Investing activities					
Property, plant and equipment and intangible assets		**(876)**	(805)	**(1,443)**	(1,431)
Long-term investments		**21**	2	**24**	2
Disposal of investments, net of divested cash and cash equivalents	6	**-**	1,669	**51**	1,831
Energy Efficiency Plan		**(35)**	(28)	**(52)**	(37)
Net disposals (acquisitions) of short-term investments		**565**	(930)	**3,050**	(707)
Other		**(1)**	(2)	**(4)**	11
		(326)	(94)	**1,626**	(331)
Financing activities					
Issuance of long-term debt		**-**	1,336	**523**	2,730
Repayment of long-term debt at maturity and sinking fund redemption		**(394)**	2	**(977)**	(661)
Redemption of long-term debt		**-**	(221)	**-**	(221)
Inflows resulting from credit risk management		**315**	380	**465**	465
Outflows resulting from credit risk management		**(625)**	(680)	**(720)**	(730)
Net change in short-term borrowings		**-**	(311)	**40**	37
Dividends paid		**-**	-	**(2,342)**	(1,126)
Other		**(1)**	(3)	**(1)**	(2)
		(705)	503	**(3,008)**	492
Change in foreign exchange on cash and cash equivalents		**(1)**	-	**(1)**	(1)
Cash flows from continuing operations		**858**	1,724	**1,084**	1,804
Cash flows from discontinued operations	6	**(1)**	268	**1**	276
Net change in cash and cash equivalents		**857**	1,992	**1,085**	2,080
Cash and cash equivalents at beginning of period		**285**	180	**57**	92
Cash and cash equivalents at end of period		**1,142**	2,172	**1,142**	2,172
Cash and cash equivalents					
Continuing operations				**1,142**	2,162
Discontinued operations				**-**	10
				1,142	2,172
Supplementary cash flow information	9				

The accompanying notes are an integral part of the consolidated financial statements.

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

In millions of Canadian dollars
(unaudited)

	Three months ended June 30		Six months ended June 30	
	2007	2006	**2007**	2006
Net income	**635**	1,442	**2,066**	2,571
Other comprehensive income				
Change in deferred gains on items designated as cash flow hedges	**256**	-	**250**	-
Reclassification to operations of deferred gains on items designated as cash flow hedges	**(31)**	-	**(76)**	-
	225	-	**174**	-
Other	**-**	-	**5**	-
Comprehensive income	**860**	1,442	**2,245**	2,571

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (unaudited)

Amounts in tables are in millions of Canadian dollars, unless otherwise indicated.

Note 1 - Basis of Presentation

The consolidated financial statements have been prepared in accordance with Canadian generally accepted accounting principles (GAAP) and reflect the decisions of the Régie de l'énergie (the "Régie"). These decisions affect the timing of the recognition of certain transactions in consolidated operations, resulting in the recognition of regulatory assets and regulatory liabilities, which the Corporation considers it is likely to recover or settle subsequently through the rate-setting process. The quarterly consolidated financial statements and the present Notes should be read in conjunction with the Consolidated Financial Statements and accompanying Notes in Hydro-Québec's *Annual Report 2006*.

The accounting policies used to prepare the quarterly consolidated financial statements conform to those presented in Hydro-Québec's *Annual Report 2006*, except as regards the changes in accounting policies described in Note 2.

Certain figures from the corresponding period of the previous year have been reclassified in order to conform to the presentation adopted in the current year.

The Corporation's quarterly results are not necessarily indicative of results for the year on account of seasonal temperature fluctuations. Because of higher electricity demand during winter months, revenue from electricity sales in Québec is higher during the first and fourth quarters.

Note 2 - Changes in Accounting Policies

On January 1, 2007, Hydro-Québec adopted the recommendations of the *Canadian Institute of Chartered Accountants (CICA) Handbook* Section 3855, "Financial Instruments – Recognition and Measurement", which states requirements for the recognition and measurement of financial instruments, and Section 3865, "Hedges", which specifies how hedge accounting may be applied and the required disclosures to be made in this context. It also adopted the recommendations of Section 3861, "Financial Instruments – Disclosure and Presentation", and Section 1530, "Comprehensive Income". This last section establishes standards for the reporting and presentation of comprehensive income, which includes net income and other comprehensive income.

Section 3855 requires that financial instruments be measured at fair value when they are initially recognized. In subsequent periods, the measurement and recognition of changes in the fair value of financial instruments depend on the category in which such instruments are classified, namely, held-to-maturity investments, loans and receivables, financial assets and financial liabilities held for trading, available-for-sale financial assets, and other financial liabilities. Accounts receivable have been classified under loans and receivables. Derivative instruments under financial assets and financial liabilities held for trading, and Short-term investments under available-for-sale financial assets. Accounts payable and accrued liabilities, Current portion of long-term debt, Long-term debt, and Perpetual debt have been classified under other financial liabilities.

All financial instruments, including derivatives, are recorded at fair value at the balance sheet date, with the exception of held-to-maturity investments, loans and receivables, and other financial liabilities, which are measured at amortized cost, that is, including premiums, discounts and issue expenses. Commodity futures that can be settled net in cash are recorded at the date of settlement if there is a probability of delivery or receipt in accordance with expected requirements.

Note 2 - Changes in Accounting Policies (continued)

Financial assets held for trading, including derivative instruments, are recorded at fair value at the balance sheet date. Gains and losses arising from changes in fair value are recognized in operations for the period during which they occur, except in the case of derivative instruments designated as hedges in a cash flow hedging relationship accounted for in accordance with Section 3865. Available-for-sale financial assets are recorded at fair value at the balance sheet date. Deferred gains and losses arising from changes in fair value are recorded in Other comprehensive income until they are realized, at which time they are reclassified to operations.

As part of its integrated risk management, Hydro-Québec applies cash flow or fair value hedge accounting to the hedging relationships that meet the conditions established in Section 3865. In the case of a cash flow hedge, the effective portion of changes in the fair value of an instrument designated as a hedge is recorded in Other comprehensive income, and the gains and losses related to the ineffective portion are immediately recognized in operations, under the same line item as the hedged item. Amounts included in Accumulated other comprehensive income are reclassified to operations, also under the same component as the hedged item, during the periods in which the change in cash flows attributable to the hedged item impacts operations. In the case of a fair value hedge, the derivative instrument is recorded at fair value, and gains and losses stemming from changes in the fair value, including those related to the ineffective portion of the hedge, are recognized in operations under the same component as the hedged item. Changes in the fair value of the hedged items attributable to the hedged risk are recognized in operations as adjustments to the hedged item's carrying amount.

In addition, an embedded derivative must be separated from its host contract and recorded at fair value on the balance sheet under certain conditions. Hydro-Québec has chosen to apply this accounting treatment to all host contracts issued, acquired or substantially modified after January 1, 2003.

Hydro-Québec also adopted the recommendations of Section 1506, "Accounting Changes", which prescribes the accounting treatment and disclosure of changes in accounting policies, changes in accounting estimates and corrections of errors.

Prior period figures have not been restated in accordance with the new accounting policies, but certain balances on the consolidated balance sheet as at December 31, 2006, have been reclassified. Derivative instruments formerly presented under Accounts receivable, Swaps, Long-term debt, Current portion of long-term debt, Accounts payable and accrued liabilities, and Accrued interest are now reclassified under Derivative instruments on the balance sheet. Translation adjustments, which formerly were presented separately in Shareholder's equity, have been reclassified to Accumulated other comprehensive income.

The impacts of adopting the new accounting policies were as follows, as at January 1, 2007:

- Retained earnings increased by $298 million, owing mainly to the abolition of transitional rules related to the application of accounting guideline AcG-13 of the *CICA Handbook*, "Hedging Relationships", to the cumulative ineffectiveness of hedges, and to the transition from the straight line method to the effective interest rate method for the amortization of financial assets and liabilities;

- Accumulated other comprehensive income increased by $479 million, owing mainly to the recording of the effective portion of cash flow hedging relationships;

- Long-term debt increased by $514 million, mainly because of the presentation at amortized cost using the effective interest rate method;

- Other long-term liabilities decreased by $2,051 million, owing to the accounting of cash flow hedging relationships, the write-off of unamortized transitional deferred gains related to the application of AcG-13, and the presentation of financial assets and financial liabilities at amortized cost using the effective interest rate method;

- A decrease of $736 million in the net value of derivative instruments, which represents the variance between the fair value of derivative instruments and the portion already recorded on the balance sheet.

Note 3 - Regulatory

TRANSMISSION

In decision D-2007-34 of March 30, 2007, the Régie set the Corporation's power transmission rates effective January 1, 2007. The new rates take into account a 7.78% return on the rate base, assuming a capital structure with 30% shareholder's equity. The impact of this decision is essentially a $57-million increase in the annual cost of native load transmission service, which has not been integrated into the Corporation's current electricity rates.

DISTRIBUTION

In decision D-2007-22 of March 15, 2007, the Régie granted an across-the-board increase of 1.92% in the Corporation's electricity rates, effective April 1, 2007. This increase takes into account a 7.79% return on the rate base in 2007, assuming a capital structure with 35% shareholder's equity.

In accordance with the accounting practices authorized previously by the Régie, variances resulting from any modification of the annual cost of native load transmission service that has not been integrated into current electricity rates, as well as cost variances related to electricity purchases in excess of the heritage pool, give rise to the recognition of regulatory assets or liabilities, with a counterparty entry in Regulatory deferrals in the Consolidated Statements of Operations. The amortization of variances relative to 2005 and 2006 began in 2007. It has yielded credits of $36 million for second quarter 2007and $72 million for the first six months of the year. These amounts are included in Depreciation and amortization in the Consolidated Statements of Operations. The regulatory asset resulting from the increase in the annual cost of native load transmission service in 2007 was $29 million at June 30, 2007, including capitalized financial expenses.

Note 4 - Depreciation and Amortization

	Three months ended June 30		Six months ended June 30	
	2007	2006	**2007**	2006
Property, plant and equipment	**451**	433	**905**	866
Intangible assets	**25**	28	**54**	57
Regulatory assets and liabilities	**(4)**	28	**(8)**	51
Deferred charges	**4**	4	**7**	8
Write-off of projects	**1**	3	**1**	3
	477	496	**959**	985

Note 5 - Financial Expenses

	Three months ended June 30		Six months ended June 30	
	2007	2006	**2007**	2006
Interest				
Interest on debt securities	**596**	579	**1,228**	1,126
Amortization of debt premiums, discounts and issue expenses	**34**	25	**61**	51
	630	604	**1,289**	1,177
Net exchange loss (gain)	**1**	(2)	**5**	(10)
Loan guarantee fees paid to the shareholder	**42**	39	**84**	79
	43	37	**89**	69
Less				
Capitalized financial expenses	**70**	76	**129**	144
Net investment income	**14**	13	**42**	20
	84	89	**171**	164
	589	552	**1,207**	1,082

Note 6 - Discontinued Operations and Assets Held for Sale

On February 28, 2007, Hydro-Québec concluded the sale of its interest in HQI Australia Pty Ltd (DirectLink), through its wholly owned subsidiary Hydro-Québec International, for a cash consideration of $52 million, which gave rise to a gain of $18 million.

In the first half of 2006, Hydro-Québec had concluded the sale of several of its foreign holdings for a total cash consideration of $2 billion, resulting in a total gain of $833 million. For purposes of segmented information, the results of foreign holdings are classified under Corporate and Other Activities.

The following table presents operating results and cash flows from the interests presented as discontinued operations:

	Three months ended June 30		Six months ended June 30	
	2007	2006	**2007**	2006
Operations				
Revenue	**-**	162	**3**	269
Income (loss) before net gain on disposal	**-**	24	**2**	23
Gain on disposal	**-**	1,030	**19**	1,082
Income taxes	**-**	(222)	**-**	(249)
Net gain on disposal	**-**	808	**19**	833
Income from discontinued operations	**-**	832	**21**	856
Cash flows				
Operating activities	**-**	152	**1**	184
Investing activities	**-**	122	**-**	107
Financing activities	**-**	(1)	**-**	(11)
Change in foreign exchange on cash and cash equivalents	**(1)**	(5)	**-**	(4)
Cash flows from discontinued operations	**(1)**	268	**1**	276

The assets and liabilities sold, as at the disposal date, were as follows:

Cash and cash equivalents	**2**	123
Other current assets	**9**	33
Long-term assets	**34**	1,935
Current liabilities	**3**	163
Long-term liabilities	**10**	1,105
	32	823

Note 7 - Financial Instruments

The fair value of derivative instruments, designated or not designated as hedges, was as follows:

	As at June 30, 2007
Instruments designated as cash flow hedges[a]	**(1,238)**
Instruments designated as fair value hedges	**(267)**
Instruments not designated as hedges[b]	**1,360**
	(145)

a) A portion of the long-term debt with a nominal value of US$1,582 million as at June 30, 2007, was also designated as a cash flow hedge.

b) Transactions carried out as part of the Corporation's risk management, including $1,206 million in consideration of amounts received or disbursed with respect to credit risk mitigation arrangements.

Effect of cash flow hedges on operations

The ineffective portion of cash flow hedges recognized in operations represented a net gain of $7 million for second quarter 2007 and a net gain of $8 million for the first six months of the year.

Moreover, as at June 30, 2007, Hydro-Québec estimated at $147 million the amount of existing net gains presented in Accumulated other comprehensive income which it expected to reclassify to operations in the next 12 months. At the same date, the maximum period over which Hydro-Québec would hedge its exposure to the variability of future cash flows for anticipated transactions was 23 years.

Effect of fair value hedges on operations

The ineffective portion of fair value hedges recognized in operations represented a negligible net loss for second quarter 2007 and a net loss of $3 million for the first six months of the year.

Effect of revaluation of instruments not designated as hedges on operations

Following the revaluation at fair value of derivative instruments which were not accounted for using hedge accounting, a negligible net gain was recognized in operations for second quarter 2007 and a net gain of $21 million was recognized for the first six months of the year.

Note 8 - Accumulated Other Comprehensive Income

	As at June 30, 2007		
	Cash flow hedges	Other	Total
Balance at beginning of period	-	(8) [a]	**(8)**
Adjustments related to the adoption of new accounting policies	479	-	**479**
Changes during the period	174	5	**179**
Balance at end of period	653	(3)	**650**

a) With the adoption of new accounting policies, $8 million was reclassified to the opening balance of Accumulated other comprehensive income as translation adjustments, which were previously presented separately under Shareholder's Equity.

Note 9 - Supplementary Cash Flow Information

	Three months ended June 30		Six months ended June 30	
	2007	2006	**2007**	2006
Change in non-cash working capital items				
Accounts receivable	**498**	609	**(250)**	(2)
Materials, fuel and supplies	**(12)**	(4)	**(18)**	(30)
Accounts payable and accrued liabilities	**(85)**	(312)	**(340)**	(551)
Accrued interest	**318**	332	**(100)**	(37)
	719	625	**(708)**	(620)
Investing activities not affecting cash				
Increase in property, plant and equipment and intangible assets	**15**	132	**28**	141
Interest paid	**193**	230	**1,122**	1,153
Income taxes paid	**-**	9	**1**	14

Note 10 - Employee Future Benefits

	Three months ended June 30			
	Pension Plan		Other plans	
	2007	2006	**2007**	2006
Accrued benefit cost	**77**	68	**24**	25

	Six months ended June 30			
	Pension Plan		Other plans	
	2007	2006	**2007**	2006
Accrued benefit cost	**153**	142	**48**	49

Note 11 - Commitments and Contingencies

Guarantees

As at June 30, 2007, the potential maximum amount Hydro-Québec could have had to pay under letters of credit and guarantees totaled $367 million. Of this amount, $289 million related to the purchase of energy, for which a liability in the amount of $19 million was recorded. Some guarantees expire between 2007 and 2019, while others do not have maturity dates.

Moreover, Hydro-Québec provided guarantees to the purchasers of its interests concerning all its representations and warranties in the sale agreements, for which no liability was recorded. The maximum quantifiable contingent risk under these guarantees is approximately $41 million. The representations and warranties of Hydro-Québec apply for a period ending no later than December 12, 2007, except with respect to the contingent tax liabilities and certain other customary representations which remain in effect until the applicable limitation periods expire.

Note 12 - Segmented Information

The following tables contain information related to operations and assets by segment:

Three months ended
June 30, 2007

	Generation	Transmission	Distribution	Construction	Corporate and Other Activities	Intersegment eliminations and adjustments	Total
Revenue							
External customers	443	9	2,297	-	8	71 [a]	**2,828**
Intersegment	1,134	698	15	537	300	(2,684)	-
Income (loss) from continuing operations	503	150	(21)	(1)	1	3	**635**
Net income (net loss)	503	150	(21)	(1)	1	3	**635**
Total assets as at June 30, 2007	28,999	15,952	11,552	270	5,412	(273)	**61,912**

a) Resales of excess supply by Hydro-Québec Distribution on outside markets are presented as offsets of electricity purchases rather than under Revenue.

Three months ended
June 30, 2006

	Generation	Transmission	Distribution	Construction	Corporate and Other Activities	Intersegment eliminations and adjustments	Total
Revenue							
External customers	477 [b]	7	2,099	-	12	-	2,595
Intersegment	986	864	13	472	283	(2,618)	-
Income (loss) from continuing operations	535	333	(261)	1	(1)	3	610
Net income (net loss)	535	333	(261)	1	831	3	1,442
Total assets as at June 30, 2006	28,009	15,689	10,681	230	8,088	(225)	62,472

b) During the quarter, a $234-million foreign exchange gain was recognized on debts and swaps denominated in U.S. dollars. In keeping with the adopted hedge accounting treatment, this amount, which represents the realization of a portion of the deferred foreign exchange gain recorded on the balance sheet, has been incorporated into other operating revenue.

Note 12 - Segmented Information (continued)

Six months ended
June 30, 2007

	Generation	Transmission	Distribution	Construction	Corporate and Other Activities	Intersegment eliminations and adjustments	Total
Revenue							
External customers	982	19	5,454	-	18	87 [a]	**6,560**
Intersegment	2,623	1,390	29	823	580	(5,445)	-
Income (loss) from continuing operations	1,410	277	372	-	(20)	6	**2,045**
Net income	1,410	277	372	-	1	6	**2,066**
Total assets as at June 30, 2007	28,999	15,952	11,552	270	5,412	(273)	**61,912**

a) Resales of excess supply by Hydro-Québec Distribution on outside markets are presented as offsets of electricity purchases rather than under Revenue.

Six months ended
June 30, 2006

	Generation	Transmission	Distribution	Construction	Corporate and Other Activities	Intersegment eliminations and adjustments	Total
Revenue							
External customers	911 [b]	16	4,849	-	19	(1)	5,794
Intersegment	2,373	1,487	27	838	543	(5,268)	-
Income (loss) from continuing operations	1,342	427	(48)	1	(9)	2	1,715
Net income (net loss)	1,342	427	(48)	1	847	2	2,571
Total assets as at June 30, 2006	28,009	15,689	10,681	230	8,088	(225)	62,472

b) During the second quarter, a $234-million foreign exchange gain was recognized on debts and swaps denominated in U.S. dollars. In keeping with the adopted hedge accounting treatment, this amount, which represents the realization of a portion of the deferred foreign exchange gain recorded on the balance sheet, has been incorporated into other operating revenue.

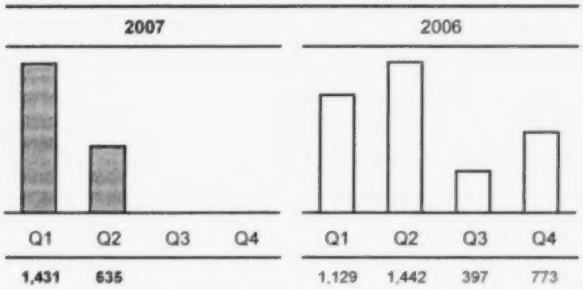
CONSOLIDATED FINANCIAL HIGHLIGHTS

In millions of Canadian dollars
(unaudited)

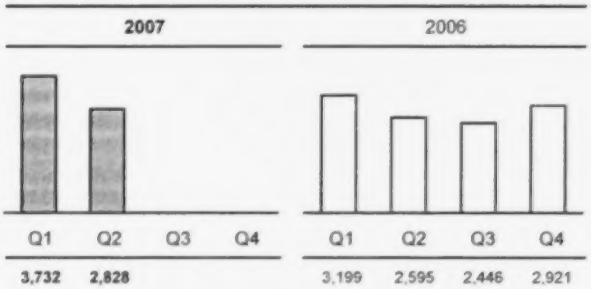
Summary of Operations

	Three months ended June 30				Six months ended June 30			
	2007	2006	Change (%)		**2007**	2006	Change (%)	
Revenue	**2,828**	2,595	9.0	↑	**6,560**	5,794	13.2	↑
Expenditure	**1,504**	1,433	11.9	↑	**3,308**	2,997	10.4	↑
Financial expenses	**589**	552	6.7	↑	**1,207**	1,082	11.6	↑
Discontinued operations	**-**	832	100.0	↓	**21**	856	97.5	↓
Net income	**635**	1,442	56.0	↓	**2,066**	2,571	19.6	↓

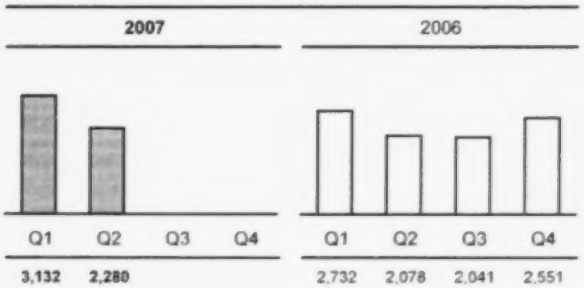
Net Income



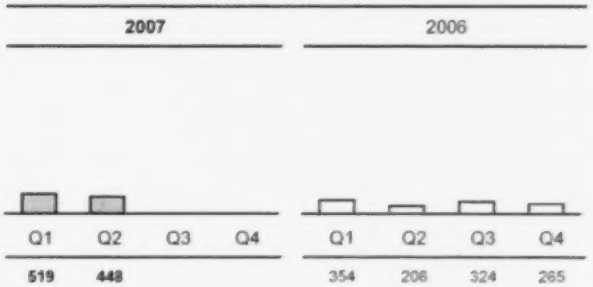
Revenue



Revenue from Electricity Sales in Québec



Revenue from Electricity Sales Outside Québec



Quarter Highlights

Transmission projects

In June, Hydro-Québec TransÉnergie held a groundbreaking ceremony for the future Outaouais substation in the municipality of L'Ange-Gardien. Hydro-Québec Équipement recently began construction on this 315/230-kV converter station after Hydro-Québec TransÉnergie signed an agreement with Hydro One Networks to establish a 1,250-MW interconnection for power interchanges between Québec and Ontario. The substation will cost an estimated $364 million and is slated for commissioning in 2009.

In April, the Régie de l'énergie authorized work on Hauterive substation. The project is designed to increase transformer capacity and to ensure long-term operability through reconfiguration of the substation equipment. This $79-million project is scheduled to come on line in stages between 2008 and 2013.

Also in April, the Régie authorized work on Sorel substation. The project consists in adding and modifying equipment to ensure system reliability, quality of service and long-term operability. It will cost $52 million and will be completed in 2010.

In June, the Régie authorized construction of Saint-Lin substation (120/25 kV) and the 120-kV Paquin–Saint-Lin transmission line. The estimated cost is $48 million, with commissioning slated for 2008.

Framework agreement

On July 13, the Régie approved the framework agreement between Hydro-Québec Distribution and Hydro-Québec Production for the period from January 1, 2007, to December 21, 2008. In approving this agreement, the Régie exempts the Distributor from going through the tendering process for very short-term supply needed to meet unanticipated demand on a real-time basis.

Mercier generating station

The first of five units at Mercier generating station in the Outaouais region was brought into service on June 29. The other units will come on line in phases until the end of the year. Mercier will have an installed capacity of 51 MW and an annual output of 0.3 TWh.

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